BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 97-009-G - ORDER NO. 97-477

JUNE 9, 1997

IN RE: Annual Review of Purchased Gas Adjustment (PGA) and Gas Purchasing Policies of South Carolina Pipeline Corporation.	) ORDER RULING ON PGA AND GAS PURCHASING POLICIES

This matter comes before the Public Service Commission of South Carolina (the Commission) on its annual review of South Carolina Pipeline Corporation's (SCPC's, Pipeline's, or the Company's) Purchased Gas Adjustment (PGA) and Gas Purchasing Policies.

Commission Order No. 87-1122 provides that an annual review be conducted of SCPC's PGA and Gas Purchasing Policies. In SCPC's last review, Order No. 96-336 in Docket No. 96-007-G dated May 13, 1996, resulted. Pursuant to the present filing, Petitions to Intervene were filed by the City of Orangeburg (the City), Lancaster, Chester, and York Natural Gas Authorities (the Authorities), the Consumer Advocate for the State of South Carolina (the Consumer Advocate), and South Carolina Electric & Gas Company (SCE&G).

A hearing was held on this matter on April 10, 1997 at 10:30 a.m. in the offices of the Commission, with the Honorable Guy Butler, Chairman, presiding. SCPC was represented by Sarena D.

Burch, Esquire and Mitchell Willoughby, Esquire. SCPC presented the testimony of Asbury H. Gibbes, Carlette L. Walker, and Jamie D. Craddock. The City was represented by James M. Brailsford, III, Esquire; the Authorities were represented by Emil W. Wald, Esquire; and the Consumer Advocate was represented by Elliott F. Elam, Jr., Esquire. The Consumer Advocate presented the testimony of Richard Hornby. SCE&G was represented by Francis P. Mood, Esquire. The Commission Staff (the Staff) was represented by F. David Butler, General Counsel. The Staff presented the testimony of Norbert M. Thomas and Brent L. Sires.

Asbury H. Gibbes testified in detail about SCPC's recent purchasing practices, concluding that it was his opinion they were prudent. Brent Sires on behalf of the Staff concurred in this conclusion. There was no evidence presented at the hearing that contradicted this testimony. Based on the foregoing, the Commission concludes that SCPC's purchasing policies and practices were prudent during the review period of February 1996 through January 1997.

Further, as explained by Mr. Gibbes, SCPC has subscribed to 75,700 mcf per day of firm transportation (FT) capacity on Transco's Sunbelt Expansion Project beginning in November 1997. We have examined this acquisition and believe that the record clearly demonstrates the need for and benefits associated with this capacity, in addition to the capacity that SCPC currently holds.

First, it appears to this Commission that the acquisition of new capacity from Transco will enable SCPC to achieve a better balance on its system between Transco and Southern Natural Gas Company (Southern). This will add further diversity and reliability to SCPC's gas supply and will promote competition among its interstate pipelines.

Second, the record reveals that the new capacity will help to ensure that sufficient capacity is available to satisfy anticipated demand requirements. According to Mr. Gibbes, SCPC expects future demand growth on its system, primarily as a result of two factors. Because of age and reliability problems with their propane air facilities, sale-for-resale customers will likely increase firm contract demand as replacement for these facilities. Additionally, significant growth in the state's economy, particularly in areas served by SCPC and SCE&G, should continue to cause expansion of the natural gas systems and increase the need for more firm capacity. In this regard, SCPC has experienced a substantial increase in peak sales volumes each year since 1991.

Third, acquisition of the additional capacity from Transco will result in a reasonable reserve margin for SCPC. It appears to this Commission that an accurate calculation of SCPC's reserve margin should reflect the time limitations associated with the capacity available from SCPC's liquefied natural gas (LNG) facilities. The record shows that, after the LNG capacity has been exhausted, SCPC's remaining reserve capacity is only around 1%. This evidence demonstrates the reasonableness of SCPC's reserve margin after including the additional Transco capacity.

Fourth, the Transco Sunbelt Expansion presented SCPC an opportunity to acquire available capacity on terms that may not be available in the future. The record shows that it would be considerably more expensive to obtain this capacity in the future. Furthermore, additional capacity will be difficult to obtain since it takes years to build new capacity, and both the Transco and Southern systems are fully subscribed, according to the record. Under these circumstances, SCPC acted prudently to obtain additional, affordable capacity from Transco.

Fifth, it would appear to this Commission that despite the testimony of Consumer Advocate witness Hornby and Staff witness Sires, it would not be prudent for SCPC to eliminate any of its existing capacity entitlements. Hornby suggested that SCPC should exercise a "regulatory out" clause in its settlement with Southern and reduce the amount of firm capacity received from the Southern system. Aside from the fact that this capacity is needed, according to the record, the elimination of capacity on Southern would produce no cost benefits. As Company witness Gibbes testified, SCPC's relinquishment of capacity would likely cause Atlanta Gas Light, Southern's largest customer, to also relinquish capacity in order to avoid resulting cost shifts. This, in turn, would shift substantially more cost to SCPC than SCPC would have avoided in reducing its Southern capacity. Moreover, Hornby admitted that he had not conducted or consulted any study or analysis to support his recommendation that existing capacity be reduced.

Sixth, considering all the benefits listed above, the cost associated with the additional Transco capacity is reasonable. Despite the Authorities' contention that costs to core customers would increase significantly, the record shows that the increase would actually be a modest one. Disregarding any credits generated through the release of capacity, the impact would be only approximately 2.8¢ per dekatherm, based on 1996 volumes.

It appears to this Commission, for all the above reasons, that SCPC's decision to acquire additional Transco capacity was reasonable under the circumstances. We believe, after examination of the concerns expressed by Consumer Advocate and Staff witnesses, that such concerns are unfounded. Hornby on behalf of the Consumer Advocate and Sires on behalf of the Staff indicated that, in their opinion, the acquisition of Transco capacity would lead to an excessive reserve margin. It appears that Hornby used 15% as a reasonable reserve margin and Sires a 29% reserve margin, the latter being a figure approved by the Commission in SCPC's PGA review two years ago. It appears to the Commission that neither figure is appropriate. The 15% reserve margin espoused by Hornby was used for planning purposes only in SCPC's Integrated Resource Plan (IRP). It does not appear to this Commission that it was intended to establish a reasonable reserve margin for SCPC. Hornby recognized this in the PGA case two years ago when he admitted that a reserve of 29% was reasonable for SCPC.

On the other hand, the Commission's finding in the earlier

PGA case that a 29% reserve margin was reasonable does not support Sires' assertion that a 29% reserve margin must be adopted in this PGA review. In the 1995 proceeding, only Hornby gave an opinion on a reasonable reserve margin, testifying that one in the range of 28 to 29% was reasonable. Once it was determined that Hornby had erroneously designated almost 8,000 dekatherms per day of gas supply as capacity and that a proper calculation resulted in a 29% reserve margin, the Commission was left with undisputed evidence that SCPC's reserve margin during the period in question was reasonable. Nothing in the Commission's Order adopted 29% as a reasonable reserve margin for SCPC or established a reasonable or particular methodology for determining a reasonable amount of reserve capacity for the future.

Moreover, in computing SCPC's reserve capacity, both Hornby and Sires improperly equated the limited capacity available from SCPC's LNG facilities with the firm transportation capacity SCPC holds on the interstate pipelines. The interstate pipeline capacity obtained from Transco and Southern is available 365 days a year. The LNG capacity, however, is severely time-limited, consisting of 90,000 mcf per day for only 10 days at Salley and 60,000 mcf per day for only 16 days at Bushy Park. Consequently, Hornby and Sires overstated the amount of SCPC's reserve capacity by assuming that the LNG capacity is the same every day of the year.

Taking into account the type and amount of capacity that is available, it is clear that Pipeline's acquisition from the

Sunbelt Expansion results in a prudent level of capacity such that SCPC can maintain and operate a reliable system 365 days a year. During those times when all of this capacity is not needed, SCPC will carry out a capacity release program to mitigate some of the cost. Although the exact amounts of capacity that could be released and revenues that would be received are unknown, SCPC has stated its belief that it will be able to conduct a successful capacity release program. SCPC has demonstrated its ability to conduct a successful hedging program to reduce volatility in gas costs. There is no reason to believe that other programs that SCPC undertakes would not be just as successful. Thus, the acquisition of the additional 75,700 mcf per day of capacity from Transco's Sunbelt Expansion Project was prudent and is therefore approved. The cost thereof is to be recovered through the weighted average cost of gas (WACOG).

We hold that there is no dispute over whether SCPC properly adhered to the tariff provisions relating to its gas costs during the review period. Company witness Carlette Walker described the procedure the Company followed for gas cost recovery, concluding that calculations had been made in accordance with the tariff and in compliance with Commission directives. Staff witness Thomas presented the Commission Staff's audit of the Company's cost of gas, verifying that the cost of gas for the review period had been properly accounted for. Finally, Staff witness Sires testified that SCPC had accurately adhered to its tariff during the period under review. Therefore, we hold that SCPC properly applied its tariff and its cost of gas was properly recovered during the review period.

With regard to capacity release, Pipeline proposed amending its tariff to allow for reduction in demand charges collected through the WACOG for revenue realized from capacity release. SCPC further proposed that 90% of such revenue be allocated to the WACOG and, as an incentive to pursue capacity release options, that 10% be retained by SCPC. The Consumer Advocate did not oppose this proposal.

The Commission Staff took issue with the proposal, both as to the method for recognizing capacity release revenue and as to the allocation. Staff's objection to the method SCPC proposed was based on the contention that existing language in SCPC's tariff is appropriate for recognizing capacity release revenue because such revenue is identified on supplier invoices as a credit or offset to demand costs. Company witness Walker explained that would not always be the case, such as when capacity is released by negotiations between the two parties. Moreover, Pipeline's proposal apparently would match these revenues to the commodity cost of gas where the costs associated with this capacity are being recovered. Further, according to Walker, the 90%-10% allocation provides an appropriate incentive for SCPC to pursue capacity release options in accordance with the trend followed in other states.

We have examined this matter, and we believe that 100% of the revenues from any capacity release should be applied to the WACOG.

Incentives as proposed by the Company are good. They will be re-evaluated in the future. However, for now, we believe that a 10% amount retained by the Company is unnecessary in order to give Pipeline an incentive for pursuing capacity release options. Pipeline should use its best efforts to release capacity. Sharing may be appropriate in the future. However, we adopt Pipeline's methodology for recognizing revenues from sales of capacity release.

With regard to unaccounted for gas, we would note, that currently, SCPC's tariff allows it to recover the cost of compressor fuel through inclusion in the WACOG. In this proceeding, SCPC proposes that the tariff be amended so that unaccounted for gas is recovered in a similar manner. This would be accomplished by amending the tariff to replace the words "compressor fuel" with "company use gas" and then to define "company use gas" as including both compressor fuel and unaccounted for gas volumes.

The Commission Staff objected to Pipeline's proposal, and recommended changing the way that SCPC recovers the cost of compressor fuel. Sires contended that the cost assigned to compressor fuel and unaccounted for gas should be calculated as average price of all gas purchases before making assignments with competitive sales pursuant to the Industrial Sales Program Rider (ISPR). (Regardless of our decision on unaccounted for gas, we believe that the evidence mandates the continuation of the ISPR program.) Sires also contended that ISPR customers should be allocated a pro rata share of compressor fuel and unaccounted for gas.

We believe that Sires first contention is inappropriate. The methodology he proposed fails to recognize that not all gas purchases actually flow to the system or are consumed during the month purchased. On a monthly basis, gas volumes are injected into underground storage facilities of the interstate pipelines or are liquefied for storage at SCPC's LNG facilities. Further, Sires' methodology contradicts the tariff provision requiring specific gas volume and cost assignments to SCPC's ISPR sales.

Second, Sires second contention is likewise inappropriate. In Order No. 90-729, the Commission specifically rejected the methodology proposed by Sires, finding that it was not appropriate to recover compressor fuel costs from the interruptible customers purchasing under the provisions of the Industrial Sales Program. The Order noted the significant benefits provided by interruptible sales and concluded that adding compressor fuel costs to these competitive, interruptible sales could inevitably reduce the volume of those sales to the detriment of all customers. There is no evidence in the record, in our opinion, that would support a departure from this prior ruling.

For similar reasons, we believe that the recovery of unaccounted for gas costs should be made through the WACOG. Sires agreed at the hearing that these costs should be recovered, and Staff admitted in its Brief that such costs are indeed gas costs. Otherwise, as Company witness Walker testified, associating the cost of compressor fuel or unaccounted for gas with competitive sales would put these sales in jeopardy and result in less industrial revenues to absorb fixed costs that would otherwise be borne by firm customers. This would contradict the policy approved by the Commission in Order No. 90-729. Further, adoption of the Commission Staff's methodology would require Pipeline to reduce its contract margin by the amount of the compressor fuel and unaccounted for gas cost and thereby constructively reduce the industrial caps established by the Commission. According to SCPC, it already loses a substantial amount of its margin pursuant to a Commission Order requiring Pipeline to reserve for the WACOG 20,000 dekatherms per day at the least expensive delivered gas cost. The Staff has recommended that this requirement be continued, and we agree, since SCPC has not objected to the continuation of this procedure. However, SCPC has submitted that additional reductions in the contract margin would not be appropriate, and we agree. We therefore adhere to our prior ruling concerning the recovery of compressor fuel costs and that unaccounted for gas be recovered by the methodology proposed by SCPC. However, both compressor fuel costs and unaccounted for gas shall continue to be reported separately.

We note that, finally, Sires stated that currently, the value assigned to compressor fuel reflects monthly demand charges contracted by SCPC. SCPC does not oppose changing the tariff so that demand charges are not associated with the value of assigned compressor fuel or unaccounted for gas volumes, provided that the

Company is permitted to continue fully recovering its actual gas costs. We hold that this should be the case.

With regard to the deferred account, SCPC initially proposed that the 90% - 10% allocation for capacity release also be used for such revenues currently held in a deferred account. Sires recommended instead that the entire account, with interest, be credited to the demand costs of gas calculation evenly over the months of October 1997 through March 1998. Staff witness Thomas calculated interest running from the date of billing to be $407,081. After reviewing Staff's recommendations, SCPC agreed at the hearing that all revenues in the deferred account should be allocated to the WACOG, with interest. SCPC, however, requested that the interest be calculated from the time that revenues were actually received, rather than the date they were billed. SCPC believes that this comports with the theory behind interest accrual on refunds, which is based on when the cash becomes available for the Company's use. This would result in the amount of interest being $394,531.21, or approximately $13,000 less than what the Staff calculated.

We hold that all revenues in the deferred account should be allocated to the WACOG with the interest figure as calculated by the Company, as we believe that interest accrual on refunds should be based on when cash becomes available for the Company's use. This should be done in installments beginning in October, 1997, through the WACOG.

With regard to the hedging program, we believe the the pilot hedging program's success since its implementation in September 1995 speaks for itself. SCPC proposed that the percentage of system supply that can be hedged be increased from 60 to 75%. Staff urged this Commission to exercise caution in increasing the percentage of system supply subject to hedging because of concerns it had about gas price volatility.

We believe that Pipeline should be allowed to increase its hedging from 60 to 75% and that the program should be continued. We think Staff's reasoning is at odds with the purpose for which the hedging proposal was instituted in the first place, that is, to manage risk and reduce the volatility of gas prices. We believe that the gas volatility theory actually supports SCPC's request to allow hedging for up to 75% of system supply. We therefore approve Pipeline's proposal.

Pipeline must file tariffs within fifteen (15) days of the receipt of this Order reflecting the findings herein made.

We have examined a number of other proposals made by the parties in this case, and hold that all other proposals not addressed specifically hereinabove and/or which are inconsistent with this Order are hereby denied.

This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Guy Butler

Chairman

ATTEST:

Gary E. Walsh

Deputy Executive Director

(SEAL)